THE WASHINGTON AND LEE UNIVERSITY
AND ITS AFFILIATE

Consolidated Financial Statements

June 30, 2014

(With Independent Auditors' Report Thereon)

THE WASHINGTON AND LEE UNIVERSITY
AND ITS AFFILIATE

June 30, 2014

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Management's Discussion and Analysis

Highlights from 2013-14

- Total endowment net assets and funds held in trust by others ended the fiscal year at a new high water mark of $1.478 billion.
- Endowment (including funds held in trust by others) per Student increased to approximately $650,000 from $585,000.
- University approved the smallest percentage increase in tuition and fees in the last fifty years with an increase of just 2.50% for the 2014-15 year.
- Completed the renovation of Robinson Hall, Gaines Hall and the IQ Center in the Science Hall. All of these projects were integral elements within the University's Strategic Plan.
- Annual Fund reached new highs in both total raised, $9.32 million, and undergraduate alumni participation, 54.7%.
- The capital campaign, *Honor Our Past, Build Our Future*, reached the $464.8 million mark toward the $500 million goal with one year remaining.
- Set new highs for undergraduate enrollment with 1,852 FTEs while law school enrollment was at 422 students. Gross tuition and fees topped $99 million while net tuition and fees revenues held steady at $59.4 million.
- University grants and scholarships were awarded to 49% of the undergraduates. Set new record number of students reached with institutional grant and scholarship support at 909 undergraduates. The percentage of undergraduates with University grants or scholarships has increased from 39% to 49% over the last six years.
- Faculty compensation, which has been strongly supported through the Lenfest Challenge, stands at 94.6% of the mean of the Top 25 peer group of schools.

A Changing Financial Model

In an industry in which most of the private liberal arts colleges throughout America are highly tuition dependent, Washington and Lee's financial model has quietly and subtly shifted away from tuition dependent toward a "philanthropic" funding model. It is in many ways a very envious position for an institution to find itself; however, it is not without its own set of challenges and management introspection. Since 2009-10, the percentage of revenues from net tuitions and philanthropic sources (endowment allocation, contributions and trusts held by others distributions) has flip-flopped. In 2009-10, net tuition accounted for 43% of all revenues while philanthropic sources accounted for 40%. This most recent fiscal year showed net tuition revenues accounting for 40% of all revenues and philanthropic sources for 43% of those revenues. As we anticipate adjusting undergraduate enrollment to more normal historic norms (closer to 1,750 undergraduate students on campus) and as the School of Law moves back to enrollments in the 300s, this gap is likely to widen. This shift has led us to begin to modify our thinking about policies and guidelines relative to endowment management to help minimize the impact of volatility and recognize the importance of downside protection within the investment portfolio.

The importance of managing and developing appropriate levels of University Reserves takes on even greater importance than it did when the University began to develop its policies several years ago. In addition, managing the endowment payout rate to moderate distributions during periods of strong investment returns in order to create greater flexibility in periods of low or negative returns within the investment markets is critical. Both have been areas of focus for the University's financial management since the economic downturn of 2008 and 2009. While management of the University believes that substantial progress has been made on these fronts, the topic remains a front burner issue as we come closer to the conclusion of the current Capital Campaign and begin focusing attention on the next strategic plan for the University.

With that as the background of management's views on the University's financial model, the following discussion provides a snapshot of Washington and Lee's financial picture and outlines how fiscal resources are utilized to provide a strong, student-centered educational experience.

Assets

Washington and Lee University experienced continued growth in assets over the past year. From $1.740 billion as of June 30, 2013, the University's assets grew to $1.918 billion as of June 30, 2014. In the past five years, the University's assets have grown by $600 million. Two areas have led this growth: endowment and plant (physical facilities) (see Fig. 1).

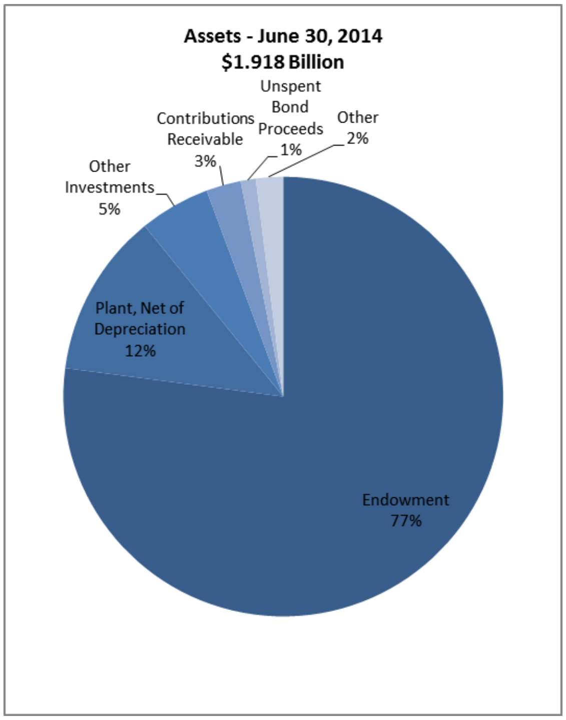

Figure 1

Endowment: Our endowment comprises two elements: gifts to the University held in the investment pool and Trusts Held by Others. The University's aggregate endowment grew to $1.478 billion at June 30, 2014 (See Fig. 2).

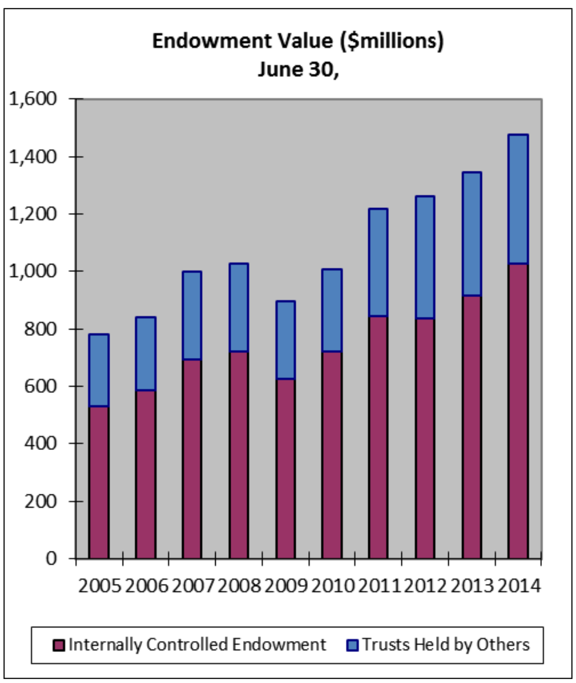

Figure 2

This was an increase from $1.345 billion as of June 30, 2013. Strong investment markets which yielded returns of 14.7% on the internally managed endowment funds and inflows of gifts more than offset the allocation from endowment for operating support of $41.6 million. Trusts Held by Others increased by $22 million while the internally held endowment grew by $110 million.

Changes in endowment value reflect gifts and additions, distributions for spending and appreciation from the underlying investment funds. For 2013-14, gifts and appreciation accounted for an increase in funds available by $152.0 million while distributions for spending totaled $41.6 million within the internally-controlled portion of the endowment. For Trusts Held by Others, appreciation accounted for $33.8 million and distributions for spending totaled $11.6 million.

Returns on a nominal basis for endowment funds with external managers exceeded the University's long-term expected return (14.7 % versus 7.5%). Over the longer term, the annual return for the ten-year period ending June 30, 2014 of 8.28% places the endowment in the top thirty percent of endowment performance (as measured by the Mellon Trust Endowment Universe). If the long-term goal of endowment management is to achieve equity-like returns at lesser volatility, then we believe that the University's Investment Committee has achieved that result since the University's endowment over the past thirty-five years has bettered the S&P 500 by 1.75% on an annual compounded basis.

Physical Facilities: The University's physical facilities represent the second largest financial investment. Unlike the endowment and trusts held by others, the University's physical plant does not appreciate over time but requires constant upkeep and preservation. At the same time, the investment in facilities is necessary to continue to create stimulating learning and social environments for our students and faculty.

During the 2013-14 year, the University finished the renovation of Robinson Hall, completing the fourth phase of the five phase renovation of the iconic Colonnade. We also completed renovations to Gaines Hall for first year student housing and the IQ Center in the Science Addition, a project that received significant funding from the Howard Hughes Medical Institute. Finally, we concluded the renovations to Belfield, the home built by Dean Frank Gilliam, which now serves as the premier guest house on the campus. As the fiscal year was ending, we began the Center for Global Learning (duPont Hall), Graham-Lees Residence Hall renovations and the second phase of fraternity housing renewal project.

Looking ahead, continued investment in facilities will be structured to meet the University's strategic objectives. Among projects anticipated over the next five years are: the final Colonnade project, Tucker Hall; renovations to Stemmons Plaza; a stand-alone Natatorium facility that will replace the pool in Warner/Doremus; a completely rebuilt Warner facility with significant improvements made to Doremus to help accommodate the additional sports teams, student populations and increases in intramural and recreational activity that have occurred on campus since Warner was constructed in the early 1970s; alterations to the law school to improve spaces to better meet the changing curricular demands of the third-year law program but also improve student-centered spaces; and finally, a new Third Year Housing community above Wilson Field.

Our approach to funding these significant projects will rely on the success of the capital campaign and the University's ability to secure more debt. It is an ambitious plan, but one that continues to build on the University's strengths and attention to our core mission.

Contributions Receivable: As the *Honor Our Past, Build Our Future* campaign continues to generate new commitments and gifts, many of them are made in the form of multi-year pledges. These play a vital role in aiding our planning efforts to ensure that we can match timing of implementation of a strategic initiative with the funding that will support it. As of June 30, 2014, contributions receivable were valued at $49.0 million. This is down from $50.1 million as of June 30, 2013 reflecting continued strong pledge payment receipts over the year.

Other Investments: The last major asset within the University's financial structure is categorized as "Other Investments". These are primarily split interest arrangements by which a donor gives the University a sum of money to invest and manage. The donor receives an income interest from these investments for a specified period of time after which Washington and Lee receives the remainder of the invested funds to support University operations. These investments totaled $78.5 million at the end of this most recent fiscal year.

Liabilities

On the other side of the ledger, the University has liabilities totaling $246.7 million. Three types of liabilities comprise 92% of this total: debt, future annuity payments and postretirement benefits. (See Fig. 3)

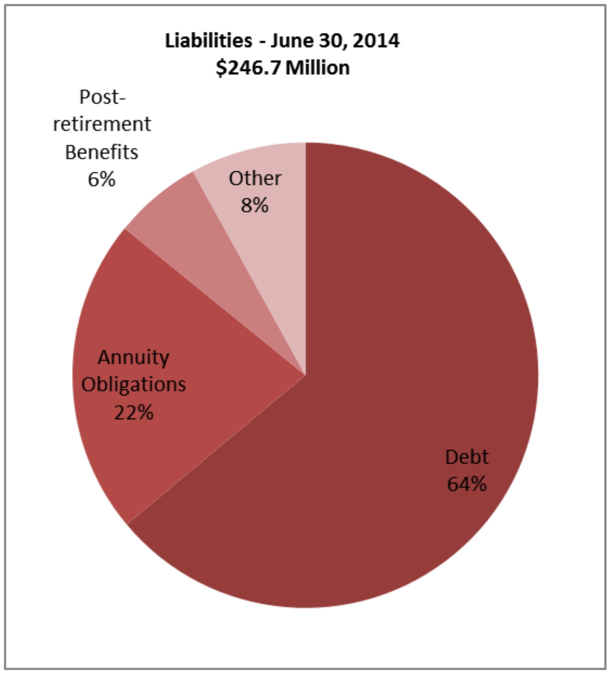

Figure 3

Debt: Washington and Lee University's largest liability is long-term debt that has been secured over the years to support capital building projects. After holding fairly constant between $120 to $135 million over the last decade (see Fig. 4), the University did take out an additional $35 million in debt in July 2013 to fund the renovation costs for the first-year housing projects and to partially fund three years of Annual Capital Projects across the campus. This has raised the outstanding long-term debt balance to $157.7 million at June 30, 2014. Over the past year, the University made $2.1 million of payments toward principal, extinguishing the 2008 Bank of America commercial note in the process, and $7.3 million in interest payments. As of year-end, the University's outstanding debt was composed of six different instruments; all being tax-exempt issues through either the Virginia College Building Authority or the Lexington City Industrial Development Authority. Of the outstanding debt, 90% is fixed rate and 10% is variable rate debt.

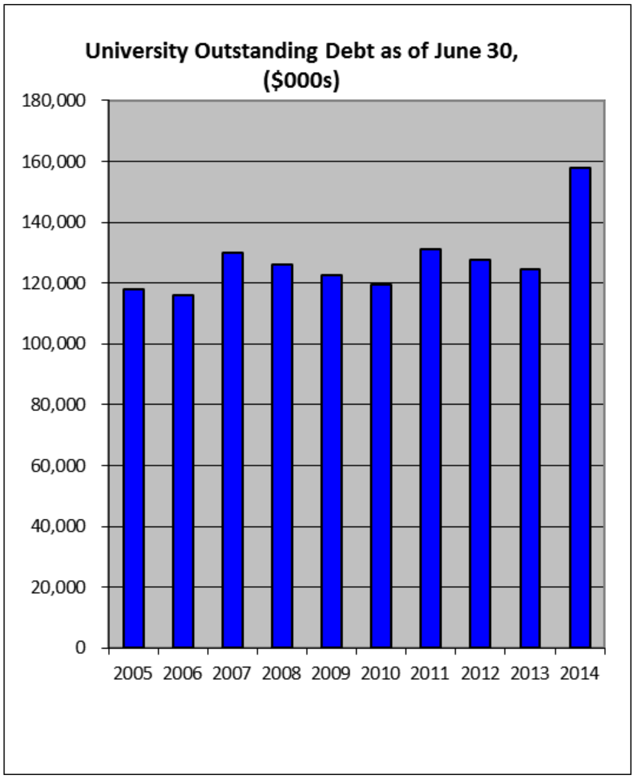

Figure 4

As part of the debt issuance process, the University has sought and maintained credit ratings with Moody's Investor Services and S&P. Currently, the University's debt is rated Aa2 and AA by Moody's and S&P, respectively. Both of these ratings reflect a "Stable" outlook from the agencies. These strong ratings reflect outside agencies' evaluations of the University's financial health and its ability to repay its obligations.

The University will most likely add debt in the next two years in support of the capital program, principally the construction of the Third-Year Housing Community. As has been our practice, we will assess appropriate debt levels and potential new debt within the context of our Debt Policy which was adopted by the Board of Trustees in 2006 to ensure that we act prudently relative to amount and structure of the debt portfolio.

Future Annuity Payments: The split interest instruments mentioned above create a liability based upon expected future payments to the donor. As of June 30, 2014, this liability was recorded at $54.1 million. It is safe to say that the University welcomes an increasing liability in this area, since it reflects a growing deferred-giving program, which will lead to greater financial support in the future.

Postretirement Benefits: Finally, the University has maintained a postretirement health benefits plan for those employees who serve 10 years or more and retire from the University. This commitment creates an annual expense for the program as well as a future obligation. This obligation, as actuarially calculated, now stands at $15.1 million, up modestly from $14.6 million at June 30, 2013. The University has altered this plan for employees hired after April 1, 2003, to shift to a defined contribution plan for employees. This will lead to an elimination of this obligation over the very long-term.

Net Assets

In the corporate world, assets minus liabilities reveal the enterprise's equity. Within higher education, this "equity" is referred to as net assets which are broken down into three components: Unrestricted Net Assets, Temporarily Restricted Net Assets and Permanently Restricted Net Assets.

Unrestricted Net Assets: These funds can be expended if necessary, and as such, they carry the greatest level of flexibility for the University to meet its long-term obligations. The build-up of these funds results from operating surpluses, the creation of quasi-endowments from large unrestricted gifts and the development of reserves over the years. With good investment markets, the University saw this class of net assets increase by nearly $25.4 million to $323.5 million at June 30, 2014.

Temporarily Restricted Net Assets: These funds are fully expendable but restricted by either a purpose, time frame for use or accumulated gains of permanently restricted endowments. Examples are gift funds restricted for support of student financial aid, gift funds to support building projects, deferred giving arrangements under which the University has an obligation to make payments to beneficiaries before receiving the remainder value to meet the donor's intent and unspent endowment allocations intended for programmatic purposes. These net assets also benefitted from a strong year of growth and finished at $443.8 million, an increase of 20% from 2013.

Permanently Restricted Net Assets: These funds are given by a donor with the express condition that the original value of the gift not be expended by the University. Instead, the funds are invested, and the University benefits from the investment return on the funds. At Washington and Lee, these funds are the underpinnings of the endowment and include many of the outside trusts that were established to be managed in perpetuity for the University's benefit. Over the past year, the value of this net asset component increased by $39.1 million to $903.5 million.

Table 1 summarizes the University's Statement of Financial Position.

Table 1

Summary	
Statement of Financial Position	
June 30, 2014 ($000s)	
Assets:	
Cash and Cash Equivalents	$ 4,842
Accounts and Notes Receivables	12,931
Contributions Receivable, net	49,027
Inventories	1,315
Investments	1,125,612
Unspent Bond Proceeds	21,238
Funds Held in Trust by Others	451,768
Assets Restricted to Investment in Plant	18,241
Land, Buildings and Equipment, net	231,418
Other Assets	1,112
Total Assets	$ 1,917,504
Liabilities:	
Accounts and Other Payables	$ 8,851
Accrued Compensation	3,768
Student and Other Deposits	765
Deferred Revenue	2,041
U.S. Government Grants Refundable	1,985
Annuity Obligations	54,134
Asset Retirement Obligations	1,236
Capital Lease Obligations	1,142
Long-term Debt	157,687
Postretirement Benefit Obligations	15,080
Total Liabilities	246,689
Net Assets:	
Unrestricted	323,487
Temporarily Restricted	443,811
Permanently Restricted	903,517
Total Net Assets	1,670,815
Total Liabilities and Net Assets	$ 1,917,504

Sources and Uses

The depth of University resources translates into the programs and services provided to students. As noted above, Endowment, Trusts Held By Others and Gifts make an enormous contribution to the revenue stream of the University and provide Washington and Lee the ability to invest in the education program. However, they are not the only revenues available to the University as Figure 5 depicts.

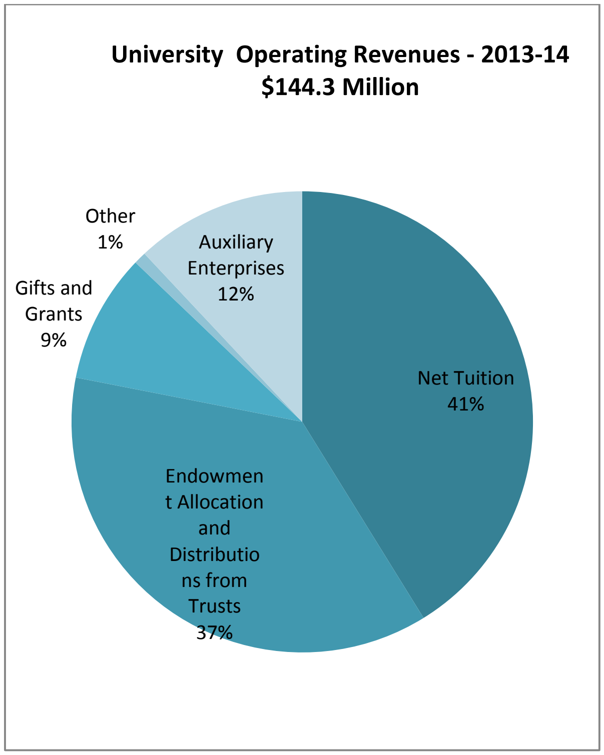

Figure 5

Tuition and fees remain the single largest source of operational support. The last five years can be characterized as modest increases in the "sticker price" for tuition at the University coupled with planned and unplanned enrollment growth. Partially offsetting this growth in enrollment and as a significant component of the Strategic Plan, we have increased financial aid to ensure that W&L can recruit the very best students possible without regard to geography, race, ethnicity, nationality or ability to pay.

In 2013-14, net tuition revenues held steady at $59.4 million. This result occurred even with a decline in the number of law students by 9% in 2013-14. On the undergraduate side, we saw the number of full-time students increase by 16 as already high retention rates showed additional improvement. Financial Aid continues to be significantly funded through endowment and gifts (48.4% in 2013-14) and provides access for students who otherwise may not be able to attend, which we believe allows the University to continue to attract the very best students.

In reading the operating results of the University (See Table 2), one must look at three pieces to understand the full commitment to Financial Aid at the University. Within revenues, Financial Aid is shown as a reduction of tuition ($39.80 million); this is also the case with Auxiliary Enterprise revenues which reflect an aid discount of $2.16

million. Finally, within the Expenses section, there is a line item for Financial Aid that totals $3.55 million. On a combined basis, student financial aid awarded by the University in 2013-14 increased at more than twice the rate of student fees (or 3.8% for student financial aid compared to 1.8% for student fees) to $45.5 million.

Table 2

Summary Statement of Activities June 30, 2014 ($000s)	
Revenues:	
Gross Tuition	$ 99,216
Less donor funded student financial aid	(22,009)
Less institutionally funded student aid	(17,787)
Net Tuition	59,420
Endowment Return Allocated to Operations	41,619
Income from Funds Held in Trust by Others	11,604
Contributions and Grants	13,072
Auxiliary Enterprises (net of $2,158 of aid)	17,296
Other	1,258
Total	**144,269**
Expenses:	
Instructional	69,007
Academic Support	18,375
Student Services	13,507
Institutional Support	18,814
Financial Aid	3,553
Auxiliary Enterprises	21,143
Other	3,619
Total	**148,018**
Operating Deficit	(3,749)
Increase in Net Assets from Non-Operating Activities	141,849
Change in Net Assets	**$ 138,100**

Endowment distributions, whether from the defined payout formula or allocations from Trusts Held by Others, accounted for 36.0% of the operating revenues in 2013-14, at $53.2 million. This source has grown in importance as a portion of the revenue stream (See Fig. 6), and as a result the diligence of management of the underlying assets and considerations of payout allocation models are as important, if not more important than a decade ago. It should be noted that prior to 2006-07, the University regularly exceeded a 5% payout from the aggregate endowment as measured against the beginning market value. In 2013-14, the endowment allocation to operations translated to a payout rate of 4.55%.

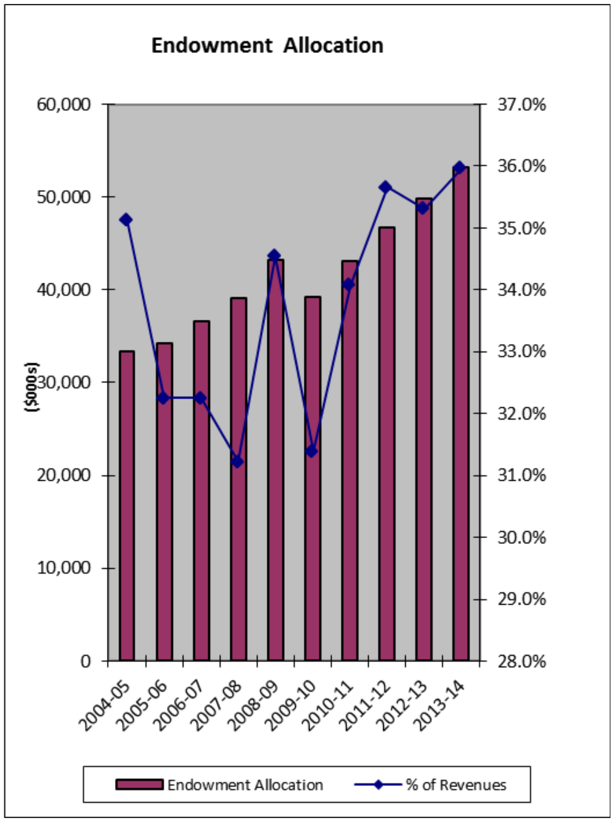

Figure 6

Current gifts and grants also play a significant role in the University's ability to provide a world-class educational program. For instance, in 2013-14, the Annual Fund exceeded $9.3 million in total commitments for the first time and reflected an increase of $600,000 from 2012-13. In addition, the University established new highs in undergraduate alumni participation with 54.7% making gifts. These unrestricted gifts underwrite all aspects of University life. In the aggregate, Washington and Lee received $13.1 million in contributions and grants in 2013-14 to underwrite operations. If the University had to rely on its endowment to generate the same level of contribution, the University would need an additional $279 million in endowment funds.

We use these resources to fulfill our core mission – education. As demonstrated in Fig. 7, Instruction and Academic Support (libraries, information technology services, etc.) comprise nearly 60% of total expenses. Fig. 7 also demonstrates that only 13% of expenditures go toward administration, including fund-raising.

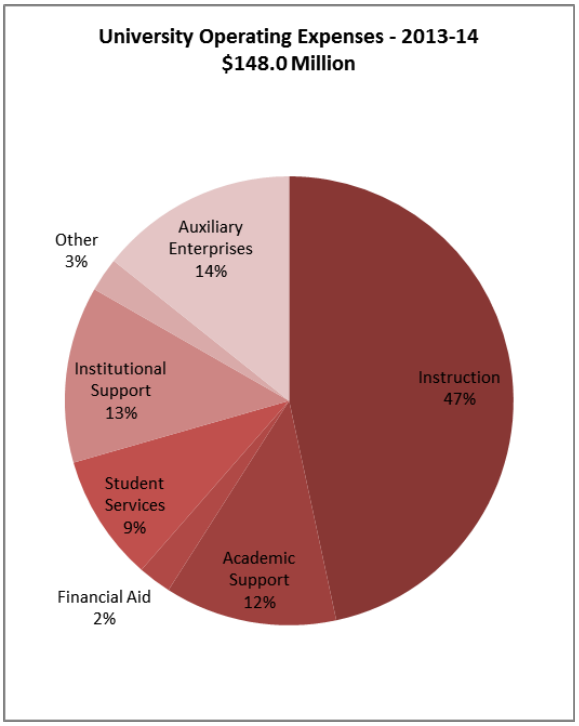

Figure 7

As in past years, comparisons of expenses within the "Top 25" group of liberal arts colleges, reveal that Washington and Lee consistently spends a higher percentage of its budget for educational expenses than the peer average (59.9% versus 52.2%). However, the University's aggregate expenses per student fall below the average expense per student of the peers by $8,350.

Results from Operations reflect an Unrestricted Operating deficit of $529,000 versus an Unrestricted Operating deficit of $95,000 in 2013. Overall, the deficit grew to $3.749 million reflecting a drawdown of temporarily restricted assets to underwrite operations. It should be noted that the University does not formally budget for depreciation expense ($12.1 million in 2013-14 allocated across the functional expenditures in Fig. 7). However, we do budget for certain similar types of activities including principal payments on debt, and annual capital projects. In addition, the Board of Trustees approved a change in the University's Reserves Policy in 2014 that, over time, should lead to an increase in the annual allocation to Capital Reserves which should be able to substitute for Depreciation budgeting. This is a long-term commitment and solution, but will help to resolve one of the perennial challenges associated with our financial modeling. Beyond these steps, we also pursue significant fundraising to support the capital program and many of these commitments are made but allocated to the project in a different year. This adjustment from temporarily restricted to unrestricted operations is made in the Non-operating activities section of the statement of activities. We believe that this comprehensive approach to facilities capital management is a reasonable and thoughtful approach, and will be considered a "best practice" model going forward.

Summary and Outlook

A strategy within the University to stay true to our mission and avoid ventures into other areas of operation has served the University and its students well over the years. It has allowed us to invest into the fundamental programs that benefit our undergraduate and law students while resonating with our alumni to secure purposeful philanthropic support. The two have gone hand-in-hand at Washington and Lee. The result is an institution that understands its identity and has been well-supported in staying faithful to that identity. During a time in higher education when many institutions deviate from their primary missions with the hopes of securing a more sustainable financial future, we have elected to "double down" on our wager. The result is reflected in the accompanying financial statements: an endowment per student that places the University in the Top 25 of all higher education institutions in America; a financial aid program that is expanding the level of accessibility to deserving students of lesser means; an academic program that strives consistently to find greater opportunities to engage students in both curricular and co-curricular activities; and an environment that prides itself on the long-lasting bonds of the relationships that are established. The cost of quality is not inexpensive, and we have recognized that managing tuition growth and providing a more financially accessible university must be achieved through gains in other resources. The success that we have seen in the *Honor Our Past, Build Our Future* Campaign has played a significant role in our ability to match priority goals with resources.

We believe we are one of the fortunate institutions in higher education today. The University's prosperity reflects both the extreme generosity of those who came before us as well as prudent but forward-looking financial management of resources. We value the underlying strength that this support has yielded for our historic University.

KPMG LLP
Suite 1010
10 S. Jefferson Street
Roanoke, VA 24011-1331

Independent Auditors' Report

The Board of Trustees
The Washington and Lee University:

We have audited the accompanying consolidated financial statements of The Washington and Lee University and its affiliate (the University), which comprise the consolidated statement of financial position as of June 30, 2014, and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the organization's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the organization's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Washington and Lee University and its affiliate as of June 30, 2014, and the changes in their net assets and their cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.

Report on Summarized Comparative Information

We have previously audited the University's 2013 consolidated financial statements, and we expressed an unmodified audit opinion on those consolidated financial statements in our report dated October 25, 2013. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2013 is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

KPMG LLP

October 27, 2014

THE WASHINGTON AND LEE UNIVERSITY AND ITS AFFILIATE

Consolidated Statement of Financial Position

June 30, 2014 (with comparative
information as of June 30, 2013)

(In thousands)

Assets		**2014**	**2013**
Cash and cash equivalents	$	4,842	9,719
Accounts and other receivables		5,837	4,778
Notes receivable, net		7,094	6,974
Contributions receivable, net		49,027	50,121
Inventories		1,315	1,254
Investments		1,125,612	1,001,512
Funds held in trust by others		451,768	429,586
Unspent bond proceeds		21,238	—
Assets restricted to investment in land, buildings, and equipment		18,241	12,697
Land, buildings, and equipment, net		231,418	222,537
Debt issuance costs, net		1,112	876
Total assets	$	1,917,504	1,740,054
Liabilities and Net Assets			
Liabilities:			
Accounts and other payables	$	8,851	7,989
Accrued compensation		3,768	3,430
Student and other deposits		765	843
Deferred revenue		2,041	2,461
U.S. government grants refundable		1,985	2,021
Split interest agreement obligations		54,134	49,707
Asset retirement obligations		1,236	1,040
Capital lease obligations		1,142	580
Long-term debt		157,687	124,707
Postretirement benefit obligation		15,080	14,561
Total liabilities		246,689	207,339
Commitments and contingencies			
Net assets:			
Unrestricted		323,487	298,093
Temporarily restricted		443,811	370,204
Permanently restricted		903,517	864,418
Total net assets		1,670,815	1,532,715
Total liabilities and net assets	$	1,917,504	1,740,054

See accompanying notes to consolidated financial statements.

THE WASHINGTON AND LEE UNIVERSITY AND ITS AFFILIATE

Consolidated Statement of Activities

Year ended June 30, 2014 (with summarized comparative information for the year ended June 30, 2013)

(In thousands)

	2014				
	Unrestricted	**Temporarily restricted**	**Permanently restricted**	**Total**	**2013 Total**
Operating revenues and gains:					
Tuition and fees	$ 99,216	—	—	99,216	97,427
Less donor funded student financial aid	(22,009)	—	—	(22,009)	(21,052)
Less institutionally funded student financial aid	(17,787)	—	—	(17,787)	(16,956)
Net tuition and fees	59,420	—	—	59,420	59,419
Endowment return allocated to operations	35,339	6,280	—	41,619	38,954
Other investment income	471	138	—	609	757
Distributions from funds held in trust by others	11,535	69	—	11,604	10,867
Contributions	10,783	—	—	10,783	10,174
Auxiliary enterprises (net of $2,158 in 2014 and $1,113 in 2013 of institutionally funded student financial aid)	17,296	—	—	17,296	18,581
Governmental and other grants	—	2,289	—	2,289	1,893
Other	399	250	—	649	439
Net assets released from restrictions	12,246	(12,246)	—	—	—
Total operating revenues and gains	147,489	(3,220)	—	144,269	141,084
Operating expenses:					
Instruction	69,007	—	—	69,007	64,820
Research	2,665	—	—	2,665	2,428
Public service	954	—	—	954	961
Academic support	18,375	—	—	18,375	16,573
Financial aid	3,553	—	—	3,553	4,704
Student services	13,507	—	—	13,507	12,757
Institutional support	18,814	—	—	18,814	19,441
Auxiliary enterprises	21,143	—	—	21,143	19,090
Total operating expenses	148,018	—	—	148,018	140,774
Change in net assets from operating activities	(529)	(3,220)	—	(3,749)	310
Nonoperating activities:					
Investment return, net of amount allocated to operations	22,105	70,541	3,178	95,824	49,824
Change in value of funds held in trust by others	—	1,769	24,142	25,911	10,895
Split interest agreements, net	12	(2,025)	(2,863)	(4,876)	(4,374)
Contributions	—	15,258	12,042	27,300	43,378
Net assets released for fixed asset acquisitions	8,039	(8,039)	—	—	—
Postretirement charge other than benefit cost	81	—	—	81	599
Other, net	(4,314)	(677)	2,600	(2,391)	74
Total nonoperating activities	25,923	76,827	39,099	141,849	100,396
Change in net assets	25,394	73,607	39,099	138,100	100,706
Net assets:					
Beginning of year	298,093	370,204	864,418	1,532,715	1,432,009
End of year	$ 323,487	443,811	903,517	1,670,815	1,532,715

See accompanying notes to consolidated financial statements.

THE WASHINGTON AND LEE UNIVERSITY AND ITS AFFILIATE

Consolidated Statement of Cash Flows

Year ended June 30, 2014 (with comparative information for the year ended June 30, 2013)

(In thousands)

		2014	2013
Cash flows from operating activities:			
Change in net assets	$	138,100	100,706
Adjustments to reconcile change in net assets to net cash and cash equivalents used in operating activities:			
Net realized and unrealized gains on investments		(131,948)	(84,659)
Depreciation and amortization		12,011	11,088
Contributions restricted for long-term investment in endowment and plant		(27,300)	(45,864)
Interest and dividends restricted for long-term investment		(1,226)	(1,300)
Changes in operating assets and liabilities:			
Accounts and other receivables, net		(1,179)	547
Contributions receivable, net		645	3,802
Inventories		(61)	(68)
Funds held in trust by others		(22,182)	(5,409)
Accounts payable and other accrued liabilities		797	(73)
Student and other deposits		(78)	134
Deferred revenue		(420)	(306)
U.S. government grants refundable		(36)	12
Split interest agreement obligations		6,360	11,073
Postretirement benefit obligations		519	(493)
Net cash and cash equivalents used in operating activities		(25,998)	(10,810)
Cash flows from investing activities:			
Purchases of land, buildings, and equipment, including interest capitalized		(19,651)	(11,237)
Purchases of investments restricted to land, buildings, and equipment		(50,966)	(19,371)
Proceeds from sale of investments		366,747	244,902
Purchases of investments		(332,455)	(240,687)
Net cash and cash equivalents used in by investing activities		(36,325)	(26,393)
Cash flows from financing activities:			
Principal payments on capital lease obligations		(207)	(145)
Interest and dividends restricted for long-term investment		1,226	1,300
Proceeds from contributions restricted for long-term investment in endowment and plant		27,749	45,864
Payments for debt issuance costs		(300)	—
Payments on split interest agreements		(4,193)	(3,894)
Proceeds from issuance of long-term debt		35,309	—
Principal payments on long-term debt		(2,138)	(2,705)
Net cash and cash equivalents provided by financing activities		57,446	40,420
Net (decrease) increase in cash and cash equivalents		(4,877)	3,217
Cash and cash equivalents:			
Beginning of year		9,719	6,502
End of year	$	4,842	9,719
Supplemental disclosure of cash flow information:			
Cash paid during the year for interest, net of amounts capitalized	$	7,331	5,755

Noncash investing and financing activities, in thousands:

At June 30, 2014 and 2013, $511 and $108, respectively, of fixed asset purchases were included in accounts payable and other accrued liabilities.

At June 30, 2014 and 2013, the University incurred capital lease obligations of $769 and $725 for equipment leases, respectively.

See accompanying notes to consolidated financial statements.

(1) Description of Organization

The Washington and Lee University (W&L) is a private, liberal arts university in Lexington, Virginia. Founded in 1749, it is the ninth oldest institution of higher learning in the nation. W&L is named after George Washington, as he gave the school its first major endowment, and after General Robert E. Lee, as a result of his strong leadership as president of W&L. W&L is comprised of the College, the Ernest Williams II School of Commerce, Economics and Politics, and the School of Law. There are approximately 1,800 undergraduate students and approximately 420 law students.

On November 15, 2010, Colonnade Restoration, LLC, a Virginia limited liability company and controlled affiliate of W&L, was formed for the purpose of restoring, rehabilitating, constructing and developing the historic buildings on W&L grounds known collectively as The Colonnade. Colonnade Restoration, LLC was formed so that the renovation expenditures incurred on the rehabilitation projects designated by the Virginia Department of Historic Resources will support Virginia Historic Tax Credits certified to Colonnade Restoration, LLC for allocation to its members. W&L has no membership interest in Colonnade Restoration, LLC but rather controls the affiliate through various leasing arrangements.

(2) Summary of Significant Accounting Policies

(a) Basis of Financial Statement Presentation and Consolidation

The consolidated financial statements include the financial statements of W&L and its affiliate Colonnade Restoration, LLC (collectively, the University). The consolidated financial statements have been prepared on the accrual basis of accounting and all significant intercompany balances and transactions have been eliminated in consolidation.

(b) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Items subject to such estimates and assumptions primarily include the carrying value of alternative investments, certain real estate holdings, post-retirement benefits, land, buildings and equipment, and accounts and contributions receivable. Actual results could differ from those estimates.

(c) Classification of Net Assets

Based on the existence or absence of donor-imposed restrictions, the University's net assets have been grouped into the following three classes:

Unrestricted – Net assets that are not subject to donor-imposed stipulations.

Temporarily Restricted – Net assets whose use is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the University pursuant to those stipulations.

Permanently Restricted – Net assets whose use is limited by donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or otherwise removed by the University.

The University classifies the portion of donor-restricted endowment funds that is not classified as permanently restricted net assets as temporarily restricted net assets until appropriated for expenditure.

The University retains an interest in several funds held in trust by others (see note 9) which are classified as permanently restricted net assets. Annual adjustments to record the University's interest in such trusts at the current market value are also recorded as permanently restricted in the consolidated statement of activities and are, therefore, reflected as permanently restricted net assets in the consolidated statement of financial position.

(d) Summarized Comparative Information

The consolidated statement of activities for the year ended June 30, 2014 is presented with certain summarized comparative information for the year ended June 30, 2013 in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with U.S. generally accepted accounting principles. Accordingly, such information should be read in conjunction with the University's consolidated financial statements for the year ended June 30, 2013 from which the summarized information was derived.

(e) Cash and Cash Equivalents

The University considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents, except those cash equivalents held by investment managers as part of their long-term investment strategy, which are included in investments.

At times during the year, the University maintains cash balances at financial institutions in excess of Federal Deposit Insurance Corporation (FDIC) limits.

(f) Inventories

Inventories are stated at the lower of cost or market with cost determined on the first-in, first-out (FIFO) basis.

(g) Investments

Investments are reported at fair value. The fair values of marketable equity and debt securities are determined using quoted market prices at the reporting date multiplied by the quantity held. The fair value of mortgage loans to exempt employees is determined as the present value of future contractual cash flows discounted at an interest rate that reflects the risks inherent in those cash flows. The discount rate approximates rates currently offered by local lending institutions for loans of similar terms with comparable credit risk. The fair values of other investments without a readily determinable fair value, such as hedge fund investments, private equity and venture capital, natural resource and real estate investments, are estimated based on the investment's net asset value of shares or units held by the University at the reporting date as a practical expedient. The various net asset values are based on valuations provided by external investment managers, which are reviewed by the University for reasonableness. Short-term investments are comprised of short-term fixed income securities valued at fair value determined from public quotations.

Purchases and sales of investments are recorded on the trade date. All investment income is reported in the period earned as unrestricted revenues, temporarily restricted revenues, or permanently restricted revenues depending on donor restrictions or law. The amount of investment income necessary to satisfy the Board of Trustees (the Board) approved spending policy for the endowment fund is included in the endowment returns allocated to operations in the consolidated statement of activities. Any excess of income earned over the approved spending amount is retained in the endowment pool.

Except for investments where donors specifically provide otherwise, investments are maintained in a pool. Gifts that are invested in the pool are assigned units of participation in the pool based upon their fair market value on the date of gift and the most recently determined unit market value for the existing units of participation. Subsequent distributions of annual income, based on the spending formula authorized by the Board, of the investment pool are based upon the number of units of participation. Withdrawals are based upon the most recently determined market value of the respective units of participation, which includes both realized and unrealized net gains or losses. The market value of the units of participation is calculated monthly.

Investments are exposed to several risks, such as interest rate, currency, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the University's consolidated financial statements.

(h) Funds Held in Trust by Others

Funds held in trust by others represent resources neither in the possession nor under the control of the University, but held and administered by outside fiscal agents, with the University deriving income from such funds. Funds held in trust by others are reported at fair value. The fair values of the assets of funds held in trust by others are based upon quoted market prices of the underlying assets held in trust at year end. The fair value of the University's share of the assets is reflected in the consolidated statement of financial position and the income (including unrealized appreciation and depreciation) is recorded in the consolidated statement of activities.

(i) Split Interest Agreements

The University is a participating beneficiary in a number of split interest agreements such as charitable remainder trusts and charitable lead trusts. Donors establish and fund a trust with specified distributions to be made to a designated beneficiary or beneficiaries over the trust's term. If applicable, liabilities to beneficiaries associated with these split interest agreements are calculated using the appropriate discount rate at the time they are established. If applicable under generally accepted accounting principles, liabilities for these split interest agreements are adjusted annually for changes in actuarial assumptions, amortization of the discount or to use a current discount rate. Upon

(Continued)

termination of the trust, the University receives the portion of assets remaining in the trust as specified by the donor.

Charitable remainder trusts, for which the University is not the trustee, are recorded at the fair value of their beneficial interest. The University records revenue for charitable lead trusts, for which the University is the trustee, based on the present value of future cash flows expected to be received by the University. The fair value of the assets held in trust by the University are included in investments and the associated liability, representing the present value of the liability to the donor's estate, is included in split interest agreement obligations in the consolidated statement of financial position.

The University also manages gift annuities, which consist of nontrust assets donated to the University in exchange for a fixed payment for a specified period of time. The gift annuities are recognized at fair value when received, and included in investments in the consolidated statement of financial position. The associated liability is initially calculated at the present value of future cash flows and adjusted in subsequent periods to reflect changes in actuarial assumptions. Liabilities associated with gift annuities are included in split interest agreement obligations in the consolidated statement of financial position.

Pooled life income funds are donated funds received by the University and are assigned a specific number of units in the pool. The donor is paid the amount of income earned on the donor's assigned units. Pooled life income funds are recorded at their fair value and are included in investments in the consolidated statement of financial position. The University's interest is recognized as contribution revenue in the period in which the assets are received by the donor. The difference between the fair value of the assets when received and the revenue recognized is recorded as a liability and included in split interest agreement obligations in the consolidated statement of financial position.

(j) Land, Buildings, and Equipment

Land, buildings, and equipment, including art properties, are stated at cost at the date of acquisition or fair value at the date of gift, less accumulated depreciation, computed on a straight-line basis over the estimated useful lives of land and building improvements (10-30 years), buildings (30-50 years), and equipment (10 years). Equipment held under capital leases is stated at the present value of minimum lease payments and amortized over the shorter of the lease term or estimated useful life of the asset. The University does not provide depreciation on its art properties because a decrease in economic benefit is not anticipated since the University expects to take the necessary steps to maintain their condition. Interest on borrowings is capitalized from the date of the borrowing until the specified qualifying assets acquired with those borrowings are ready for their intended use or the borrowing is retired, whichever occurs first. Capitalized interest is amortized over the useful life of the qualifying asset.

(k) Recognition and Classification of Gifts

Contributions of cash and other assets, including unconditional promises to give, are recognized as revenue when the gifts are received by the University. Gifts are reported in the appropriate category of net assets in the consolidated statement of activities, except contributions that contain donor-imposed restrictions that are met in the same fiscal year. Gifts whose restrictions are met in the same fiscal year as their receipt are reported as unrestricted contribution revenue.

The University records gifts of cash and other assets as restricted support if they are received with donor-imposed restrictions or stipulations that limit their use. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions.

The University reports gifts of land, buildings, and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support.

In the event a donor makes changes to the nature of a restricted gift which affects its classification among the net asset categories, such amounts are reflected as "redesignated funds" in the consolidated statement of activities.

Unconditional promises to give that are expected to be collected within one year are recorded on the date of gift at net realizable value which approximates fair value. The University uses present value techniques to measure the fair value on the date of gift of unconditional promises to give that are expected to be collected in future years. The discount rates used to compute the discounts on those amounts are determined at the time the unconditional pledges are initially recognized and are not revised subsequently. Amortization of the discounts is recorded as additional contribution revenues in accordance with the donor-imposed restrictions on the contributions. Subsequently, an allowance is made for uncollectible contributions based upon management's judgment after analysis of creditworthiness of the donors, past collection experience, and other relevant factors.

Conditional promises to give are not recognized as revenues until such time as the conditions are substantially met. The aggregate fair value of the conditional pledges received by the University is indeterminable as of June 30, 2014.

(l) Asset Retirement Obligations

The University has asset retirement obligations arising from regulatory requirements to perform certain asset retirement activities associated with the cost of removal and disposal of asbestos and fuel tanks. The liability was initially measured at fair value and subsequently is adjusted for accretion expense and changes in the amount or timing of the estimated cash flows. The corresponding asset retirement costs are capitalized as part of the carrying amount of the related long-lived asset and depreciated over the asset's remaining useful life.

(m) Tuition and Fees and Auxiliary Revenue

Student tuition and fees and auxiliary revenue are recognized as revenue during the fiscal year in which the related academic services are rendered. Student tuition and fees and auxiliary revenue received in advance of services to be rendered are reported as deferred revenue in the consolidated statement of financial position. Student tuition and fees and auxiliary revenue are recorded in the consolidated statement of activities net of student financial aid provided to the student by the University. Student financial aid is provided from earnings on restricted funds and certain board-designated endowments, along with gifts and grants dedicated to providing student financial aid.

(n) Functional Expenses

The University has developed and implemented a system of allocating expenses related to more than one function. These expenses are depreciation, interest and operations and maintenance of plant. Depreciation is allocated by individual fixed assets to the function utilizing that asset. Interest is allocated based on the use of borrowed money in the individual functional category. Allocation of operations and maintenance of plant expenses was determined through a study of departmental uses of the operations and maintenance budget within each functional category.

(o) Operations

The University classifies revenues earned and expenses incurred related to its core missions of teaching, research and scholarship, and investment returns made available for current use as operating revenues or expenses in the consolidated statement of activities. All other activities, including contributions restricted by donors or designated for longer term use by the Board, are shown as a component of nonoperating activities.

(p) Derivative Instruments

All derivative instruments are recognized as either assets, included in accounts and other receivables, or liabilities, included in accounts and other payables, in the consolidated statement of financial position at their respective fair values. Changes in the fair value of derivative instruments are recorded as other non-operating activities on the consolidated statement of activities. Using derivative financial instruments may increase the University’s exposure to credit risk and market risk. The University minimizes the credit (or repayment) risk in derivative instruments by (1) entering into transactions with high-quality counterparties, (2) limiting the amount of exposure to each counterparty, and (3) monitoring the financial condition of its counterparties. Market risk is the adverse effect on the value of a derivative financial instrument that results from a change in interest rates.

(q) Income Taxes

The Washington and Lee University has been classified as an organization described under Section 501(c)(3) of the Internal Revenue Code and thus exempt from federal income taxes on activities related to its exempt purpose. The University does not believe that there are any unrecognized tax benefits or costs that should be recorded in the consolidated financial statements. Accordingly, no provision for income taxes has been reflected in the consolidated financial statements.

The Internal Revenue Service has held that a Virginia limited liability company, treated as a partnership for state income tax purposes, would also be treated as a partnership for federal income tax purposes. Therefore, income taxes are not provided with respect to the operations of Colonnade Restoration, LLC since each member is responsible for the income tax consequences associated with its proportionate share of such operations.

(r) Fair Value Measurements

Certain assets and liabilities are reported or disclosed at fair value in the consolidated financial statements. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The University utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. The University determines fair value based on assumptions that market participants would use in pricing an asset or liability in the principal or most advantageous market. When considering market participant assumptions in fair value measurements, the following fair value hierarchy distinguishes between observable and unobservable inputs, which are categorized in one of the following levels:

- Level 1 Inputs: Unadjusted quoted prices in active markets for identical assets or liabilities accessible to the reporting entity at the measurement date.
- Level 2 Inputs: Other than quoted prices included in Level 1 inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability.
- Level 3 Inputs: Unobservable inputs for the asset or liability used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at measurement date.

See note 7 for additional information with respect to fair value measurements.

(3) Notes Receivable

Notes receivable are carried at unpaid principal balance, less an allowance for doubtful accounts, and consist of the following at June 30, 2014 and 2013 (in thousands):

	Maturity	Interest rates		2014	2013
Student financial aid:					
Federally funded aid, net of allowance for doubtful accounts of $294 and $258, respectively	up to 10 years	3% – 5%	$	2,047	1,630
University funded aid, net of allowance for doubtful accounts of $311 and $259, respectively	up to 10 years	3% – 9%		3,349	3,268
Other notes:					
Note receivable from sale of property	10/31/2020	5%		1,628	1,839
Miscellaneous notes	various	various		70	237
			$	7,094	6,974

(4) Contributions Receivable

Contributions receivable, which are reported net of an allowance for uncollectible amounts and a present value discount, are expected to be collected as follows at June 30, 2014 and 2013 (in thousands):

		2014	2013
Less than one year	$	25,072	23,724
One year to five years		24,227	26,150
Over five years		1,038	1,647
Total contributions receivable, gross		50,337	51,521
Less allowance for uncollectible contributions		(497)	(513)
Total contributions receivable, net of allowance		49,840	51,008
Discount (rates ranging from 0.1% to 7.67%)		(813)	(887)
Total	$	49,027	50,121

(5) Land, Buildings, and Equipment

Land, buildings, and equipment at June 30, 2014 and 2013 consist of the following (in thousands):

		2014	2013
Land	$	5,730	5,730
Land improvements		10,502	10,176
Buildings and improvements		333,568	316,707
Equipment		46,919	43,855
Art properties		3,451	3,147
		400,170	379,615
Less accumulated depreciation and amortization		(173,507)	(161,584)
		226,663	218,031
Construction in progress		4,755	4,506
Total	$	231,418	222,537

(6) Investments

Investments are comprised of the following at June 30, 2014 and 2013 (in thousands):

		2014	2013
Short-term investments	$	37,412	34,419
Equities		184,641	129,576
Fixed income		58,184	46,692
Real assets		65,364	62,713
Hedge funds		2,691	2,635
Mortgage loans to staff and fraternities		46,659	44,978
Multi-Asset Class (see below) *		699,476	647,181
Private equity/venture capital		31,185	33,318
Total	$	1,125,612	1,001,512

* This represents the University’s investments in Makena Capital Management, LLC (Makena). Makena’s Multi-Asset Class portfolio is diversified across geographies, strategies, and over 140 investment managers.

(Continued)

The following table summarizes the investment return and its classification in the consolidated statement of activities (in thousands):

		2014	2013
Interest and dividend income, net of investment expenses of $1,099 and $821 in 2014 and 2013, respectively	$	6,104	4,876
Net appreciation in fair value of investments		131,948	84,659
Total investment return		138,052	89,535
Less investment return available under spending policy, including unrestricted amounts of $35,339 and $33,335 in 2014 and 2013, respectively, and temporarily restricted amounts of $6,280 and $5,619 in 2014 and 2013, respectively		(42,228)	(39,711)
Investment return in excess of amount available under spending policy	$	95,824	49,824

The University maintains a statement of investment policies and objectives which is approved by the Investment Committee and the Board of Trustees. The policy, which is reviewed no less than every two years, provides guidance on investment objectives, appropriate investment vehicles, asset allocation and spending policy for the endowment investments. In December 2007, the University employed Makena to manage the majority of the University's endowment funds. In so doing, the University has delegated the authority for asset allocation and manager selection to Makena, and in the period since the selection of Makena, the University has redeemed holdings from other managers (legacy investments) and placed those funds with Makena. As of June 30, 2014, approximately 68% of the University's endowment funds were held at Makena.

Makena utilizes both traditional and nontraditional investment strategies for the implementation of asset allocation. The single investment pooled fund is invested in approximately 141 individual managers across 7 asset classes and over 46 sub-asset class investment strategies. The portfolio is structured across the asset and sub-asset classes to generate performance in excess of relevant benchmarks while realizing substantially lower volatility than equity markets.

The portfolio as of June 30, 2014 and 2013 was allocated across the following asset classes as follows:

	2014	2013
Equity	15%	12%
Tactical hedged equity	9%	10%
Real estate	11%	11%
Private equity	20%	21%
Natural resources	8%	10%
Absolute return	22%	25%
Fixed income	8%	10%
Cash	7%	1%

The University has within its investments, those investments held by the University as trustee that provide payout to named beneficiaries but will ultimately be passed to the University. These funds are held at BNY Mellon and are invested primarily across a range of equity indexed products and fixed income indexed products in a more traditional investment approach. The majority of the funds are held in mutual fund products.

The following table summarizes the University's investments in entities that calculate net asset value as practical expedient to estimate fair value as of June 30, 2014, as well as liquidity and funding commitments (in thousands):

	2014			
	Fair value	Unfunded commitments	Redemption frequency (if currently available)	Redemption notice period
Real assets	$ 65,364	—	*	*
Multi-Asset Class	699,476	—	Annual	1 year
Private equity/venture capital	31,185	1,452	*	*

* These are primarily limited partnerships where distributions are made to investors through the liquidation of the underlying assets. It is expected to take 10-12 years to fully distribute these assets.

(7) Fair Value Measurements

(a) Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of the University's financial instruments.

- **Cash and cash equivalents, student accounts receivables, other receivables, unspent bond proceeds, assets restricted to investment in land, building, and equipment, accounts payable, other payables, and accrued liabilities:** The carrying amounts approximate fair value because of the short maturity of these financial instruments.

- **Notes receivable:** The University has estimated the net realizable value of notes receivable, evaluated collection history, and has concluded the carrying amount approximates fair value.
- **Contributions receivable and split interest agreement obligations:** The University has estimated the net realizable value of contributions receivable and split interest agreement obligations, and has concluded the carrying amounts approximate fair value. The discount rates used in calculation of split interest agreement obligations ranged from 1.2% to 10.6% at June 30, 2014 and 2013.
- **Investments and funds held in trust by others:** The fair values of marketable equity and debt securities are determined using quoted market prices at the reporting date multiplied by the quantity held. The fair value of mortgage loans to exempt employees is determined as the present value of future contractual cash flows discounted at an interest rate that reflects the risks inherent in those cash flows. The discount rate approximates rates currently offered by local lending institutions for loans of similar terms with comparable credit risk. The fair values of other investments without a readily determinable fair value, such as hedge fund investments, private equity and venture capital, natural resource and real estate investments, are estimated based on the investment's net asset value of shares or units held by the University at the reporting date as a practical expedient. The various net asset values are based on valuations provided by external investment managers, which are reviewed by the University for reasonableness. Short-term investments are comprised of short-term fixed income securities valued at fair value determined from public quotations.

  Although the fair values of the assets of funds held in trust by others are based upon quoted prices at year-end, funds held in trust by others are categorized as Level 3 assets in the fair value hierarchy due to the University's lack of control over the trusts.
- **Interest rate swaps:** The fair value of interest rate swaps is determined using pricing models developed based on the LIBOR swap rate and other observable market data, adjusted to reflect nonperformance risk of both the counterparty and the University.
- **Long-term debt:** The estimated fair value of the University's long-term debt was $181,031,000 and $137,821,000 as of June 30, 2014 and 2013, respectively. Fair values for 2014 and 2013 were estimated based on an average interest rate of 2.49% and 2.96%, respectively, the bond buyer municipal index rate for June 30, 2014 and 2013. Using the remaining principal amortization structure of each series of bonds and interest rates, a calculation was performed to get a bond yield and then a discount rate for each existing series of bonds. Each discount rate was then used to calculate the present value of debt service, reflecting average interest rates that are slightly above current rates for similar indebtedness. These inputs are considered Level 2 in the fair value hierarchy.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the University believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

(b) Fair Value Hierarchy

The following table presents assets and liabilities that are measured at fair value on a recurring basis at June 30, 2014 (in thousands):

	Total June 30, 2014	Fair value measurements at reporting date using		
		Level 1	Level 2	Level 3
Assets:				
Investments:				
Short-term investments	$ 37,412	30,123	7,289	—
Equities	184,641	184,600	—	41
Fixed income	58,184	58,038	20	126
Real assets	65,364	—	3,761	61,603
Hedge funds	2,691	2,691	—	—
Mortgage loans to staff and fraternities	46,659	—	46,659	—
Multi-Asset Class	699,476	—	—	699,476
Private equity/venture capital	31,185	—	—	31,185
Total investments	1,125,612	275,452	57,729	792,431
Funds held in trust by others	451,768	—	—	451,768
Total assets	$ 1,577,380	275,452	57,729	1,244,199
Liabilities:				
Interest rate swaps	$ 56	—	56	—

The University’s investment with Multi-Asset Class manager (Makena) is reported as a Level 3 investment; however, it is estimated that the underlying portfolio is structured such that the assets as they would report would be allocated with 22% in Level 1, 8% in Level 2 and 70% in Level 3 as of June 30, 2014.

There were no significant transfers between Level 1 and Level 2 investments for the year ended June 30, 2014.

The following table presents assets and liabilities that are measured at fair value on a recurring basis at June 30, 2013 (in thousands):

	Total June 30, 2013	Fair value measurements at reporting date using		
		Level 1	Level 2	Level 3
Assets:				
Investments:				
Short-term investments	$ 34,419	34,127	292	—
Equities	129,576	129,558	—	18
Fixed income	46,692	46,598	19	75
Real assets	62,713	—	4,411	58,302
Hedge funds	2,635	2,635	—	—
Mortgage loans to staff and fraternities	44,978	—	44,978	—
Multi-Asset Class	647,181	—	—	647,181
Private equity/venture capital	33,318	—	—	33,318
Total investments	1,001,512	212,918	49,700	738,894
Funds held in trust by others	429,586	—	—	429,586
Total assets	$ 1,431,098	212,918	49,700	1,168,480
Liabilities:				
Interest rate swaps	$ 75	—	75	—

The University's investment with Multi-Asset Class manager (Makena) is reported as a Level 3 investment; however, it is estimated that the underlying portfolio is structured such that the assets as they would report would be allocated with 13% in Level 1, 10% in Level 2 and 77% in Level 3 as of June 30, 2013.

There were no significant transfers between Level 1 and Level 2 investments for the year ended June 30, 2013.

The University owns interests in alternative investment funds rather than in the securities underlying each fund, and therefore it is generally required to consider such investments as Level 2 or 3, even though the underlying securities may not be difficult to value or may be readily marketable. Because net asset value is used as a practical expedient to estimate fair value, the level in the fair value hierarchy in which each fund's fair value measurement is classified is based primarily on the University's ability to redeem all or a portion of its interest in each fund at or near the date of the consolidated statement of financial position. Accordingly, the inputs or methodology used for valuing or classifying investments for financial reporting purposes are not necessarily an indication of the risk associated with investing in those investments or a reflection on the liquidity of each fund's underlying assets and liabilities.

The following table presents the University's activity for assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended June 30, 2014 and 2013 (in thousands):

		Investments	Funds held in trust by others	Total
Beginning balance at June 30, 2012	$	674,122	424,177	1,098,299
Net realized and unrealized gains		67,132	21,762	88,894
Net purchases (maturities)		895	(5,486)	(4,591)
Distributions		(3,255)	(10,867)	(14,122)
Ending balance at June 30, 2013		738,894	429,586	1,168,480
Net realized and unrealized gains		91,424	37,515	128,939
Net purchases (maturities)		316	(3,729)	(3,413)
Contributions		51	—	51
Distributions		(38,254)	(11,604)	(49,858)
Ending balance at June 30, 2014	$	792,431	451,768	1,244,199

For the years ended June 30, 2014 and 2013, there was approximately $116,177,000 and $78,027,000, respectively, of net unrealized gains included in the change in net assets that were attributable to Level 3 assets still held at June 30, 2014 and 2013.

(8) Endowment

Endowment is a term used commonly to refer to the resources that have been restricted by donors or designated by the Board of Trustees that will be invested to provide future revenue to support the University's activities. As of June 30, 2014, the University holds 1,254 endowment funds, of which 1,162 are true endowments (restricted by the donor) and 92 are quasi-endowments (designated by the Board).

(a) Interpretation of Relevant Law

Based on the interpretation of Virginia's legislation, which incorporates the provisions of the Uniform Prudent Management of Institutional Funds Act (the Act or UPMIFA), by the Board of Trustees of the University, and absent explicit donor stipulations to the contrary, the University classifies the original value of gifts donated to the permanent endowment, as well as accumulations to the permanent endowment made at the direction of the donor, as permanently restricted net assets.

The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Board of Trustees in a manner consistent with the standard of prudence prescribed by the Act. In accordance with the Act, the University considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: the duration and preservation of the fund; the purposes of the University and the donor-restricted endowment fund; general economic conditions; the possible effect of inflation or deflation; the expected total return from income and the appreciation of investments; other resources of the University; and the investment policies of the University.

Endowment net assets consist of the following at June 30, 2014 (in thousands):

		Unrestricted	Temporarily restricted	Permanently restricted	Total
Donor-restricted endowment funds	$	(1)	344,667	438,795	783,461
Board-designated endowment funds		242,694	—	—	242,694
Total endowed net assets	$	242,693	344,667	438,795	1,026,155

Endowment net assets consist of the following at June 30, 2013 (in thousands):

		Unrestricted	Temporarily restricted	Permanently restricted	Total
Donor-restricted endowment funds	$	(442)	277,511	423,726	700,795
Board-designated endowment funds		214,975	—	—	214,975
Total endowed net assets	$	214,533	277,511	423,726	915,770

Changes in endowment net assets for the years ended June 30, 2014 and 2013 are as follows (in thousands):

		Unrestricted	Temporarily restricted	Permanently restricted	Total
Endowment net assets, June 30, 2012	$	197,027	246,747	393,602	837,376
Investment return:					
Investment income		687	1,162	—	1,849
Net appreciation		19,473	59,406	—	78,879
Contributions and pledge payments		6,422	70	30,124	36,616
Appropriation for expenditure		(9,076)	(29,874)	—	(38,950)
Endowment net assets, June 30, 2013	$	214,533	277,511	423,726	915,770
Investment return:					
Investment income		1,169	2,811	—	3,980
Net appreciation		31,218	96,355	—	127,573
Contributions and pledge payments		5,279	103	15,069	20,451
Appropriation for expenditure		(9,506)	(32,113)	—	(41,619)
Endowment net assets, June 30, 2014	$	242,693	344,667	438,795	1,026,155

(b) Funds with Deficiencies

From time to time, the fair value of assets associated with an individual donor-restricted endowment fund may fall below the original value of the fund. Deficiencies of this nature that are reported in unrestricted net assets were $1,000 and $442,000 as of June 30, 2014 and 2013, respectively. Subsequent gains that restore the fair value of the assets of the endowment fund to the required level will be classified as an increase in unrestricted net assets.

(c) Return Objectives and Risk Parameters

The University has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets.

(d) Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, the University relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The University targets a diversified asset allocation that places emphasis on investments in equities, bonds and absolute return strategies to achieve its long-term return objectives within prudent risk constraints.

(e) Spending Policy and How the Investment Objectives Relate to Spending Policy

The Board-approved spending formula for the endowment provides for spending the lesser of the prior year allocation incremented by a Consumer Price Index-based inflator, 6% of the three-year average of fair values at June 30, or a 5% ceiling related to the June 30 fair value. This model is often referred to as a constant growth spending formula. The calculated spending rate was 4.68% and 4.79% for June 30, 2014 and 2013, respectively.

(9) Funds Held in Trust by Others

The majority of the funds held in trust by others comes from Letitia P. Evans' bequest of 15% of the annual net income of the Lettie Pate Evans Foundation, Inc. Restricted Fund. At June 30, 2014 and 2013, the fair value of the University's interest was reported by the trustees as $407,863,000 and $386,245,000, respectively. During the years ended June 30, 2014 and 2013, the University received distributions of $10,747,000 and $9,893,000, respectively, from the Lettie Pate Evans Foundation, Inc. Restricted Fund.

At June 30, 2014 and 2013, the University maintained an interest in 41 other trusts with fair values reported by the trustees of approximately $43,905,000 and $43,341,000, respectively, and received distributions for the years ended June 30, 2014 and 2013 of $857,000 and $974,000, respectively.

(10) Long-Term Debt and Derivative Instruments

Long-term debt consists of the following obligations at June 30, 2014 and 2013 (in thousands):

	Final maturity	Interest rates	2014	2013
Virginia College Building Authority (VCBA):				
1998 Note, includes unamortized premium of $1,007 and $1,066, respectively (A)	January 2031	5.03% – 5.05%	$ 53,212	53,271
2001 Note, includes unamortized premium of $1,909 and $2,009, respectively (B)	January 2034	5.00% – 5.75%	44,909	45,009
2006 Note, includes unamortized premium of $241 and $261, respectively (C)	January 2016	4.00% – 5.00%	8,841	10,231
Industrial Development Authority of the City of Lexington, Virginia (Lexington Authority):				
2003 Note (D)	April 2018	Variable	988	1,251
2010 Note (E)	January 2035	Variable	14,440	14,595
2013 Note, includes unamortized premium of $337 (F)	January 2043	4.88%	35,297	—
Bank of America				
2008 Commercial Note	January 2014	2.76%	—	350
			$ 157,687	124,707

(A) Semi-annual interest payments on this note began July 1, 1998 with annual principal payments commencing on January 1, 2022 and continuing until maturity in January 1, 2031.

(B) Semi-annual interest payments began January 1, 2002 with annual principal payments commencing January 1, 2016 and continuing until maturity in January 2034.

(C) Annual principal and semi-annual interest payments on this note began January 1, 2007. The 2006 Bonds may not be called for redemption at the option of the VCBA before January 1, 2016. 2006 Bonds maturing on or after January 1, 2017, may be redeemed at the option of the VCBA with direction of the University prior to their respective maturities in whole or in part at any time, on or after July 1, 2016.

(Continued)

(D) Principal payments on this note are due in installments of $65,833 on each January 1, April 1, July 1 and October 1, beginning July 1, 2003 and continuing until April 1, 2018. Interest on the unpaid principal is payable on these same dates at a variable annual rate equal to the sum of (a) 65% of the LIBOR and (b) 0.59%. The interest rates for the year ended June 30, 2014 ranged from 0.69% to 0.72%.

(E) Annual principal and semi-annual interest payments on this note began January 1, 2012 and will mature January 1, 2035. The 2010 Bonds may be called for redemption upon notification by the University to the Lexington Authority. These bonds have been structured as variable rate demand bonds with a weekly reset. The interest rates for the year ended June 30, 2014 ranged from 0.03% to 0.12%.

(F) In July 2013, the Lexington Authority issued bonds in the amount of $34,960,000. The proceeds derived from the sale were loaned to the University in exchange for its Note. Such proceeds were used primarily to finance the renovations of Gaines Hall, Graham-Lees Dorms, and landscape improvements to the adjoining courtyard providing housing for first year students, and projects pursuant to the University's Annual Capital Plan, including but not limited to: small-scale renovations and improvements of buildings, technology replacements and upgrades, vehicle replacements, campus landscaping, and athletic field and facility improvements. These bonds have been structured at a fixed rate of 4.88%. Semi-annual interest payments on this note began January 1, 2014 and will mature on January 1, 2043. The bonds are subject to redemption prior to maturity upon notification by the University to the Lexington Authority, in whole or in part, at any time on or after January 1, 2022, upon payment of 100% of the principal amount of the bonds to be redeemed plus interest accrued to the date fixed for redemption. At June 30, 2014, approximately $21 million of proceeds from the 2013 bond issuance remained unspent. This amount is included in unspent bond proceeds in the consolidated statement of financial position.

Aggregate principal payments due for the next five fiscal years are: 2015 – $1,868,000; 2016 – $4,148,000; 2017 – $3,924,000; 2018 – $4,058,000; 2019 – $4,060,000; and thereafter – $136,135,000.

<u>Revolving Credit Agreement</u>

The University has a Revolving Credit agreement with Branch Banking and Trust Company that permits the University to borrow through April 20, 2016 up to $14,595,000, bearing interest at an adjusted LIBOR rate by adding 30-day LIBOR plus one and one-quarter of one percent (1.25%) per annum; however, the interest rate shall not be less than two and one-quarter of one percent (2.25%). The University paid an origination fee of $5,000 for access to this liquidity. At June 30, 2014, the University had $14,595,000 available under this facility.

<u>Interest Rate Swap Agreements</u>

From time to time, the University enters into interest rate swap agreements with financial institutions to effectively convert the variable interest rates on a portion of its outstanding Notes to a fixed rate of interest. The fair values of the University's interest rate swaps at June 30, 2014 and 2013 (liabilities in both years) were $56,000 and $75,000, respectively, and changes in the fair values (gain in both years) of those swaps for the years ended June 30, 2014 and 2013 were $19,000 and $56,000, respectively.

(11) Net Assets

(a) Temporarily Restricted Net Assets

Temporarily restricted net assets at June 30, 2014 and 2013 are available for the following purposes (in thousands):

		2014	2013
Financial aid	$	8,345	7,783
Faculty support		1,916	2,224
Program support		26,308	26,914
Buildings and equipment		19,385	13,726
Contributions receivable, for program support		31,683	31,661
Planned giving arrangements		13,062	12,164
Other		1,139	746
Accumulated appreciation on donor-restricted endowment funds, principally for program support and financial aid		341,973	274,986
Total	$	443,811	370,204

(b) Permanently Restricted Net Assets

Permanently restricted net assets at June 30, 2014 and 2013 are comprised of the following (in thousands):

		2014	2013
Purpose restricted:			
Financial aid	$	261,414	252,138
Faculty support		37,728	35,668
Program support		560,709	534,126
Library and collections support		4,503	4,165
Buildings and equipment		4,566	3,617
Other		6,684	6,636
		875,604	836,350
Time and purpose restricted:			
Contributions receivable		17,925	19,315
Planned giving arrangements		9,988	8,753
		27,913	28,068
Total	$	903,517	864,418

(Continued)

(c) *Net Assets Released from Restrictions*

Net assets are released from donor restrictions when expenses are incurred to satisfy the restricted purposes or by occurrence of other events as specified by donors. Purpose restrictions accomplished during the year ended June 30, 2014 were as follows (in thousands):

Financial aid	$	1,426
Program support		7,072
Other		3,748
		12,246
Buildings and equipment		8,039
Total	$	20,285

(12) Expenses

Expenses for the years ended June 30, 2014 and 2013 were incurred for the following (in thousands):

		2014	2013
Salaries, wages and benefits	$	88,982	84,800
Supplies and services		34,936	34,347
Depreciation and amortization of buildings and equipment		12,135	11,274
Costs of sales, auxiliary enterprises		4,713	5,038
Interest		7,252	5,315
Total	$	148,018	140,774

(13) Retirement Plans

Academic and nonacademic personnel of the University are included in the 403(b) contributory retirement plan of the Teachers Insurance and Annuity Association and College Retirement Equities Fund (TIAA-CREF) and Fidelity Management Trust Company (Fidelity). The University matches optional employee contributions up to 5% of their annual salary. In addition, the University makes a mandatory contribution of 5% of the employee’s annual salary. Contributions are paid currently to TIAA-CREF or Fidelity. The University’s cost under this plan amounted to approximately $5,633,000 and $5,404,000 for the years ended June 30, 2014 and 2013, respectively.

The University also maintains a discretionary defined contribution retirement plan through TIAA-CREF. The Washington and Lee Retiree Health Plan (the Plan) exists for the purpose of providing postretirement medical benefits to eligible academic and nonacademic personnel of the University. Employer contributions for the years ended June 30, 2014 and 2013 totaled $74,000 and $108,000, respectively.

(14) Postretirement Benefits

The University currently provides health insurance in the form of a retiree medical benefit (the Plan) to certain retired employees and their dependents. The costs of postretirement benefits are accrued during the service lives of employees. Employees of record prior to April 1, 2003 are eligible to qualify for this benefit. Those hired on or after April 1, 2003 cannot participate in the Plan. The Plan is unfunded.

The components of net periodic postretirement benefit cost for the years ended June 30, 2014 and 2013 were as follows (in thousands):

		2014	2013
Service cost (benefits attributed to employee service during the year)	$	327	379
Interest cost on accumulated postretirement benefit obligation		659	566
Amortization of prior service cost		92	155
Net periodic postretirement benefit cost	$	1,078	1,100

The amortized actuarial gain results from changes in certain assumptions and will be amortized over a period based on the average future service of participants expected to receive plan benefits.

The discount rates used in determining the accumulated postretirement benefit obligation (APBO) as of June 30, 2014 and 2013 were 4.25% and 4.50%, respectively. The assumed health care cost trend used in measuring the accumulated postretirement benefit obligation was 8% in 2014, decreasing to 5% over the next ten years.

The following information summarizes activity in the unfunded postretirement benefit plan for the years ended June 30, 2014 and 2013 (in thousands):

		2014	2013
Change in benefit obligation:			
Accumulated benefit obligation, beginning of year	$	14,561	15,054
Service cost		327	379
Interest cost		659	566
Actuarial loss (gain)		10	(769)
Net benefits paid		(477)	(669)
Accumulated benefit obligation, end of year	$	15,080	14,561
Amount not yet recognized in net periodic benefit cost and included in unrestricted net assets:			
Net actuarial gain	$	(1,935)	(2,007)
Prior service cost		619	773
	$	(1,316)	(1,234)

Projected postretirement health benefits expected to be paid in each of the next five fiscal years are: 2015 – $635,000; 2016 – $778,000; 2017 – $920,000; 2018 – $1,009,000; and 2019 – $1,125,000. An additional $7,019,000 is expected to be paid for the fiscal years 2020 through 2024.

Total employer and participant contributions are $477,000 and $71,000, respectively, for the year ended June 30, 2014. Total benefits paid for the year ended June 30, 2014 are $548,000. The employer and participant contributions for the year ending June 30, 2015 are expected to be $537,000 and $98,000, respectively, for a total of $635,000 in benefits paid. The expense discount rates for the year ended June 30, 2014 and 2013 were 4.50% and 3.75%, respectively. The measurement date was June 30, 2014.

(15) Commitments

The University's contractual commitments for capital expenditures totaled approximately $22,935,000 at June 30, 2014, and were comprised of the following (in thousands):

Center for Global Learning	$	9,243
Residence halls, sorority, and fraternity upgrades		9,112
Law School renovations		1,604
Athletic facility upgrades		1,187
Various other projects		1,789
	$	22,935

(16) Concentration Risk

Financial instruments that potentially subject the University to concentration of risk consist primarily of an equity investment in a large U.S. company. This investment comprised 87% and 86% of total funds held in trust by others as of June 30, 2014 and 2013, respectively.

(17) Contingencies

The University receives revenues under U.S. Government grants and contracts. The ultimate determination of amounts received under these programs generally is based upon allowable costs, which are subject to audit, and are reported to the U.S. Government. Recovery of indirect costs is based on predetermined rates negotiated with the government. The University is of the opinion that adjustments, if any, arising from such audits will not have a material effect on the consolidated financial statements.

From time to time, the University is involved in various legal proceedings which are in the normal course of operations. In management's opinion, the University is not currently involved in any legal proceedings which individually or in the aggregate could have a material effect on the financial condition, change in net assets and/or liquidity of the University.

(18) Subsequent Events

The University has evaluated subsequent events for potential recognition and/or disclosure in the June 30, 2014 consolidated financial statements through October 27, 2014, the date the consolidated financial statements were issued, and determined that there are no other items to disclose.